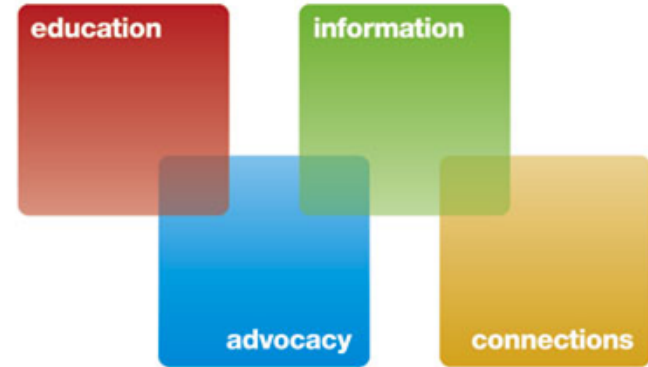




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Illinois Office of the Comptroller Financial Training Workshop 2016



Agenda

- Selecting An Auditor
- What To Look For In An Audit
 - Required Communications With Management And Those Charged With Governance
- Questions To Ask Your Auditor
- Basic Internal Control Measures



Selecting An Auditor

- External Auditor Selection/Evaluation Criteria
 - A. Industry experience
 - B. Access to specialized technical resources
 - C. Independence
 - D. Reasonableness of scope/fee
 - E. Ability to communicate/useful recommendations
 - F. Project Management
 - G. Quality control procedures
 - H. Audit team chemistry



Selecting An Auditor

A. Industry Experience

- Local government clients
- Different industries (i.e. governments, insurance, employee benefit plans, etc.)
- Significant audit areas (i.e. investments, capital assets, pensions, etc.)

B. Specialized resources

- Information technology
- Tax Increment Financing (TIFs)
- Pensions Self-insurance
- Debt financing



Selecting An Auditor

C. Independence

- Applies to the engagement team, the firm's local office, and in some cases the firm as a whole, consider:
 - Business relationships
 - Family relationships
 - Accounting and other non-audit services

D. Reasonableness of scope/fee

- Audit scope should be reasonable for the government
 - Taking a controls approach vs. a substantive approach
- Require both hours and staff levels by major audit area
- Beware of unusually low competitive bids



Selecting An Auditor

E. Ability to Communicate Useful Recommendations

- Ask relevant questions to evaluate the partner's ability to communicate and respond to inquiries from the audit committee or those charged with governance
- Require frequent, open communication with:
 - management
 - the audit committee or those charged with governance, in accordance with the auditors' professional standards
- Require feedback on how your organization can be more effective and efficient, ask for suggestions for best practices



Selecting An Auditor

F. Project Management

- Inquire of amount of planned interim vs. field work
- Inquire of level of partner and manager involvement in the planning stages of the audit
- Inquire as to whether reviews by the partner and manager are completed when the audit team is in the field
- Inquire as to how the audit process is managed
 - Communication plan
 - Status meetings
 - Overruns



Selecting An Auditor

G. Quality control procedures

- Is there a secondary partner review with adequate skills to provide value to the team?
- Has the firm obtained a peer review report and if so, did the firm pass that review?
- What internal procedures does the firm have in place to ensure a quality audit?

H. Audit Team Chemistry

- Professional and courteous
- Appropriate level of professional skepticism
- Appropriate communication skills



What To Look For In An Audit

- Auditors should provide written reports/letters on:
 - Audited Financial Statements (F/S)
 - Required Communications to the Board (Board Letter)
 - Main areas covered:
 1. Auditor's responsibility in relation to the F/S audit
 2. Other information & documents containing audited F/S
 3. Planned scope & timing of the audit
 4. Compliance with all ethics requirements regarding independence
 5. Significant accounting policies adopted in the current year
 6. Significant accounting policies which will be applicable in future years
 7. Significant accounting estimates



What To Look For In An Audit

➤ Required Communications to the Board (Board Letter)

○ Main areas covered (cont.):

8. F/S disclosures
9. Identified or suspected fraud, if applicable
10. Significant difficulties encountered during the audit
11. Uncorrected and corrected misstatements
12. Accounting services
13. Disagreements with management
14. Representation requested from management
15. Management consultations with other accountants
16. Other significant matters, findings or issues



What To Look For In An Audit

- Control Deficiencies Letter (Management Letter)
 - Major internal control weaknesses, if any, will be identified with recommendations for improvements
 - Other comments may cover minor internal control weaknesses
 - Advice to improve operations
 - Management responses to address issues with time frame for completion
- Compliance Audit
 - Federal single audit
 - TIFs
 - Grant audits



Questions To Ask Your Auditor

- Sample Questions Related to the Issued Reports:
 - A. Audited Financial Statements
 - Were there any significant changes in financial statement amounts from the prior year? (See MD&A)
 - What were the significant estimates and underlying management assumptions we should be aware of?
 - Are there any modifications to the auditor's report
 - Has your firm been engaged to provide any non audit services?
 - B. Required Communications with the Board (Board Letter)
 - Is there anything going on in the organization that you are uncomfortable with or consider unusual, or that warrants further investigation?



Questions To Ask Your Auditor

C. Control Deficiency Letter

- Would you please describe the ideas you have discussed with management for improving the internal control system over financial reporting?

D. General Questions

- Are you aware of any anticipated event that could possibly impair the independence, in fact or in appearance, of your firm and any of your staff?
- Were any integrity or honesty concerns noted?
- Are there any red flags indicating financial distress for the entity?



Questions To Ask Your Auditor

D. General Questions (cont.)

- Has management, legal counsel, or others made you aware of anything that could be considered a violation of laws, regulations, Generally Accepted Accounting Principles, professional practice, or other ethics?
- Was management prepared for the audit?
- Are there any questions we have not asked that should have been asked? If so, what are those questions?



Basic Internal Control Measures

- What is Internal Control?
- Three Types of Internal Controls:
 - Those that affect the reliability of financial reporting
 - Those that affect the effectiveness and efficiency of operations
 - Those that affect compliance with applicable laws and regulations
- Five Interrelated Internal Control Components:
 - A. Control Environment – Tone at the top
 - B. Risk Assessment
 - C. Control Activities
 - D. Information & Communication
 - E. Monitoring



Basic Internal Control Measures

A. Control Environment – Tone at the Top

- Factors Affecting Control Environment:
 - Integrity and Ethical Values
 - Commitment to Competence
 - Board or Council Participation
 - Management's Philosophy and Operating Style
 - Organizational Structure
 - Assignment of Authority and Responsibility
 - Human Resource Policies and Practices



Basic Internal Control Measures

B. Risk Assessment

- Risks can arise or change due to the following:
 - Changes in Operating Environment
 - New Personnel
 - New or Revamped Information Systems
 - Rapid Growth
 - New Technology
 - New Services or Activities
 - Restructuring
 - Accounting Pronouncements



Basic Internal Control Measures

C. Control Activities

- Controls that may be categorized as Policies & Procedures that pertain to the following:
 - Performance Reviews
 - Information Processing
 - Physical Controls
 - Segregation of Duties
- Types of Control Activities:
 - Preventive Controls
 - Detective Controls



Basic Internal Control Measures

D. Information & Communication

- An Information System encompasses methods and records that:
 - Identify and Record
 - Describe on a Timely Basis
 - Measure the Value
 - Determine the Time period
 - Present Properly



Basic Internal Control Measures

E. Monitoring

- Monitoring of controls is a process to assess the effectiveness of internal control performance over time
 - Regular management and supervisory activities
 - Internal audits
 - Monitoring of IT generated exception reports



Basic Internal Control Measures

Fraud Prevention and Detection

- Fraud Prevention Examples:
 - Segregation of duties
 - Adherence to organizational policies & procedures especially on documentation & authorization of transactions
 - Regular internal reviews and independent audits of areas more susceptible to fraud
- Fraud Detection:
 - Independent reconciliations
 - Inspections of documents (canceled checks)
 - Problems detected by audits



Questions?

